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THE BANK OF CANADA, AND GENERAL BUSINESS

ROSS B. WILLIS, M.A.

ONE of the most important pieces of legislation enacted by the Parliament of the Dominion of Canada in many years, perhaps since Confederation, was the Act incorporating the Bank of Canada, assented to on July 3 of this year. The preamble of this statute[1] sets out as the *raison d'etre* and the objectives of this institution which will take its place as the pivotal point of the financial organization of Canada, the following:—

> "to regulate credit and currency in the best interests of the economic life of the nation, to control and protect the external value of the national monetary unit and to mitigate by its influence fluctuations in the general level of production, trade, prices and employment, so far as may be possible within the scope of monetary action, and generally to promote the economic and financial welfare of the Dominion."

To The Bank of Canada, hence, as is apparent from the above, has been delegated, along with its other duties, the extremely grave responsibility of promoting stability in the commodity price level and in general business conditions in the Dominion. Canadian business men, naturally, will wish to consider the implications of this objective and it is the the purpose of this article to discuss, in a brief manner, the factors involved in the carrying out of such a duty, the efficacy of a central bank in achieving the same, and the limitations confronting such an effort.

CENTRAL BANKS—THE ORTHODOX POINT OF VIEW

Kisch and Elkin in their admir-

1. *Statutes of Canada, 24-25, George V, chap. 43—"An Act to Incorporate the Bank of Canada".*

able work, "Central Banks", have declared that:—

> "The essential function of a central bank is the maintenance of the stability of the monetary standard. This involves the control of the monetary circulation and the bank, therefore, should be given the right of note issue and preferably the sole right."

This, the traditional and orthodox pre-war view of the functions of a central bank, has been elaborated upon by Dr. B. M. Anderson of the Chase National Bank of New York to include the following objectives:

> 1. "It is the business of a central bank to protect the paper money of the country by converting it into gold on demand. This is its first and most essential function and everything else must be subordinated to this.
>
> 2. "It is the business of a central bank to ease off monetary stringencies and to prevent business crises from degenerating into money panics. In a crisis, the central bank supplies whatever money is necessary at a steep discount rate. It enables solvent men to protect their solvency but it does not regard it as its duty to validate the unsound assets of really insolvent men or to help defer the liquidation of stale positions.
>
> 3. "In times of great speculative excesses, whether in commodities or in securities, central banks should attempt to prevent the extension of unsound credit, to protect the liquidity of the banks of the country, and to check speculative excesses by tightening the money market.
>
> 4. "It is not the business of a central bank to finance a boom —least of all, a stock market boom."

Upon the basis of this point of view, a central or reserve bank is charged with the grave responsibility of being a countervailing force and a stabilizing influence in the money market—a task undoubtedly requiring extreme sagacity and foresight and courage of both conviction and action. Its major emphasis, accordingly, must be upon guaranteeing the stability of the monetary standard and its general operations must be carried out with this consideration in mind. Little is said or implied, however, as to the central bank's responsibility for commodity prices or the state of business conditions within the country, except insofar as they may be concerned with the monetary or banking position.

METHODS OF CONTROL

In order to make the above policies effective, a central bank usually possesses three media of

control, of varying effect and influence at different stages of the business cycle. These devices of control may be enumerated as follows:

The Discount Rate

The discount rate is the rate of interest charged by the central institution upon advances or discounts of the type eligible for the granting of such accommodation by the central or reserve bank. The theory underlying the influence of the discount rate, holds to the hypothesis that fluctuations in this rate affect not only the borrowing by the commercial banks from the central bank, but also the interest rates upon all short-term loans and discounts in the country. Hence, an advance in the rate of discount should serve to check the volume of borrowing and curb extension of credit by the commercial banks to commerce and industry.

Inasmuch as it is the accepted conception that commercial banks should not be continuous borrowers at the central institution but rather use it as an emergency reservoir, the discount rate normally is kept slightly above the open market rate for similar transactions.

Because short-term loans, and bills of exchange, which represent the accommodation granted by central banks, move very freely between financial centres, the relative level of rates as between these centres is important. Under normal conditions, the raising of the discount rate in one centre causes an increased flow of funds to that centre to take advantage of the higher rate, and a decline in the export of the funds from this centre. If the country is on a gold basis, gold tends to be imported and, if not, the exchange rate tends to move more favourably in the direction of that market.

Because of the fact that in most countries, the commercial banks are not continuous borrowers at the central or reserve bank, an increase in the rate of discount may be ineffectual in curbing the extension of credit by the former, unless they feel willing and able to co-operate. Hence, the weapon of the discount rate may be quite an empty symbol unless the commercial banks have begun to seek accommodation at the central reservoir, or unless they operate under self-directed or statutory, uniform policies with regard to reserves, or unless they are willing to accept the dictates of the central authority.

An increase in the rate of interest charged by the central bank on advances or discounts possesses its greatest power when the volume of credit in the country is well ex-

panded. It is worthy of note, however, that the power of an increase in the discount rate was nullified very greatly in the United States before the stock market debacle, through the fact that speculation had been permitted to reach excessive levels and, through the pouring into the money market of private and corporate funds on a large scale, over the direction of which the Federal Reserve Board had little control.

The effectiveness of a lowered discount rate also may be dissipated very materially by the existence of a fear psychology on the part of not only the commercial banks but also of borrowers in general. The complete breakdown of confidence which has been such a prominent manifestation during the present depression has served to explode in a very considerable measure the omnipotence of the discount rate of the central or reserve bank, particularly in this respect.

Moral Suasion

Should the weapon of the discount rate have little or no influence upon conditions in the money market, other media are within the power of the central bank in order to make its policy effective. By public statements and conferences, or what is commonly known as "moral suasion," an attitude of caution and conservatism may be engendered in the general community by the central or reserve bank.

This medium of control, however, must be used in a very sparing manner and unless there has grown up a respect for the policy of the central or reserve institution, propaganda of this nature may be entirely ineffectual. Although this method of control has been attempted several times in the United States by the Federal Reserve Board, it never has assumed the potency with which it fundamentally is possessed because of a lack of respect in certain quarters for the organization and administration of this body. As a result of this lack of respect, several warnings by the Federal Reserve Board in 1929 went entirely unheeded.

On the other hand, the persuasive powers of the Bank of England have reached an exceptional degree of perfection. The age and reputation of "The Old Lady of Threadneedle Street" and the small number of banks with which it is forced to deal and its failure to publish its official policy, have created a tradition which has proved very effective, insofar as moral suasion is concerned.

In the final analysis, this weapon has an influence of a psychological character solely, and its potency

is predicated entirely upon the respect which the central or reserve bank has been able to engender in the minds of the commercial banking fraternity, and in business and industry in general.

Open Market Operations

The third device open to a central bank, that of open market operations, is, in reality, a supplementary one designed to aid in making the discount rate more effective. The state of the exchanges, excessive speculation or other unhealthy symptoms of trade, may indicate the necessity for a restriction in credit, at a time when the reserves of the commercial banks are sufficiently large to make them virtually independent of the central institution. At such a time, a mere increase in the discount rate, already out of touch with market conditions, would be fruitless in bringing about such a restriction. If, therefore, the central bank seeks to reduce the market supplies of money, a potent corrective is applied by the liquidation by the central institution on its own account of large quantities of bills or securities held.

The payment for these has the effect of reducing the resources of the commercial banks and of transferring them to the central bank. The process has to be continued only until the rate of discount of the central institution becomes effective, so that it is again in a position to dominate the market. Because of the fact that the cash reserves of commercial banks are but an insignificant amount in the total volume of their credit, a diminution of these reserves quickly causes them to effect a policy of credit contraction, and the influence is magnified many fold in the ultimate results.

Conversely, the acquisition of bills and securities by the central bank, by which the cash of the commercial banks is increased, may be of great assistance in time of sudden stringency in relieving the strain upon the commercial banking institutions. The securities utilized in these operations are usually early-maturing Government securities, treasury bills or certificates of indebtedness and sometimes bills of exchange.

In order that this device may be effective, the commercial banks must maintain a rather fixed relationship between the amount of their reserves and the volume of their credit outstanding. Otherwise, the policy of the central or reserve institution can be countered in a very unusual degree. At a time when the central bank was attempting to effect an expansion of credit on the part of the commercial banks, an insistence by them upon permitting the reserves

created by the central bank through open market purchases to pile up, would counter very greatly the policy decided upon by the central authority.

This particular condition was demonstrated very forcefully in the United States during the year 1932, when the gigantic purchases of United States Government securities by the Federal Reserve Banks, merely caused the piling up of idle funds in the larger money centres, because of the refusal or inability on the part of the member banks in those centres, to expand their loaning operations on a profitable basis. A similar situation occurred in Canada in the latter part of the same year, when advances aggregating $35,000,000 were made to the chartered banks of Canada, under the Finance Act, with as one of its avowed purposes, an expansion of loaning operations on their part.

The utilization of this particular medium of open market transactions, of course, presupposes the holding by the central bank of a considerable amount of securities, or bills of exchange, which can be utilized for this purpose, and that selling operations shall be limited to such holdings.

LIMITATIONS PLACED UPON CONTROL

Certain of the difficulties confronting the operations of a central bank in carrying out the functions of monetary management and credit control were alluded to in the preceding section and these may well be summarized at this juncture. In the first place, an inelasticity in the demand for bank credit at certain stages of the business cycle must be recognized. During particular periods of the depression, business refuses to borrow regardless of the rate, because of an absence of profit-making possibilities with respect to any accommodation secured. In addition, the past decade or two has seen the development of a mass of other investing institutions, whose volume of funds is not particularly variable but over the direction of which, the central bank possesses but little control. Furthermore, a very great limitation is placed upon central bank control as the consequence of the problems involved in using the right device of control at the right time, and unless this be done the entire course of action which the central institution has adopted may meet with disaster.

A loss of confidence in the commercial banking system, as exemplified in the United States during the early part of 1933, may render almost negative any control which the central or reserve banking institution possesses over the credit

system of the country. Again, as was demonstrated in Great Britain, after the return to the gold standard in 1925, fundamental economic conditions not only in the domestic country but abroad, and foreign credit policies, may place in the path of a particular central bank difficulties of an almost insurmountable character.

As a consequence of the above, it would seem evident that the control of a central bank in monetary management and credit possesses distinct limitations. In recent years, however, there has been an increasing development of a view that the powers of a central bank in directing national destiny, are unlimited. It has been argued in certain quarters, particularly in the United States, where legislation such as the Strong Bill and the Goldsborough Bill have crystallized the idea, that a central bank has within its grasp such omnipotence that it can, of its own accord, create prosperity or adversity, and thus, by judicious administration, it may maintain prosperity indefinitely.

CENTRAL BANK INFLUENCE ON COMMODITY PRICES AND THE NEW CONCEPTION OF CENTRAL BANKING CONTROL

The Goldsborough Bill, defeated by the Senate of the United States in 1932, proposed that the credit policy of the Federal Reserve Banks should be guided by commodity prices and it would have directed the Federal Reserve Board to raise the general level of commodity prices at wholesale, to the average levels of 1921-1929 and to keep them there. Whether this would have been judicious is quite another question, although it should not be forgotten that despite an almost stable commodity price level during this period with a slight decline at times, the United States suffered the greatest depression probably in its entire history. The Goldsborough Bill presupposed that the Federal Reserve System could not only raise the commodity prices to the level for the years 1921-1929 but that after this had been accomplished it would be possible by central bank action completely to stabilize them merely by an expansion or contraction of Federal Reserve bank credit.

In order to attempt to answer the question as to whether central banks have within their power the media effectively to control commodity prices, it is necessary to recognize at the outset that central bank influence on commodity prices can be achieved only through the effect of central bank policy upon the money and capital markets, and that, furthermore, central bank policy is but one of many factors

operating in these two particular markets.

The influence which a central bank may exercise upon the money and capital markets of a country has been outlined by Dr. B. M. Anderson in the Chase Economic Bulletin of May 16, 1932, as follows:

"There are five main sources of capital:

(1) Consumers' thrift.

(2) The turning back of business profits, including corporate profits, to industry and trade.

(3) Taxation, when the proceeds of the taxes are used for capital purposes and very especially for the purpose of reducing public debt.

(4) Direct capitalization, as when a farmer spends his spare time in building barns and fences, or putting in sub-soil drainage, or when a farmer allows his herds and flocks to grow instead of selling off the annual increase.

(5) New bank credit, the product of bank expansion, based on excess bank reserves, which may grow out of

(a) inflowing gold, or

(b) increased central bank credit.

"The money market proper is the market where bank deposits are exchanged for highly liquid loans, namely acceptances, call loans in the Stock Exchange, open market commercial paper, prime customers' commercial paper of short maturity, and so on. The capital market is the market where liquid funds are exchanged for bonds, for real estate mortgages, for corporate shares, for real estate itself, and for other slow, less liquid, and more risky investments.

"Rates of interest in the capital market and in the money market depend upon both supply and demand. There are many subdivisions in each of these markets, each with its own special supply and demand, and each with its own special rate or rates.

"Normally, rates will be lower for the most liquid loans. Normally, rates in the money market will be lower than rates in the capital market, and normally, there will be gradations and differentials in each of these markets, favouring the shorter, safer, and more liquid loan or investment.

"What is the power of central bank policy with respect to money and the capital market?

"First, its direct influence is only on the money market. It can influence the capital market only indirectly as it first affects the money market. Second, in its influence on the money market, it can affect only the supply side. Demand it cannot con-

trol. Taking money market and capital market together, it can affect the supply side of only one of the five main sources of capital, namely bank credit. Investors' savings, corporate savings, Government policy with reference to the paying off of public debt, and direct capitalization are all beyond the control of the central bank.

"Even in the regulation of commercial bank expansion or contraction, central bank credit is only one of five major influences, the other four being

(a) international movements of gold,

(b) the confidence of the people, as manifested in their willingness to deposit their cash in the banks or their preference for hoarding cash,

(c) the confidence of the bankers, as manifested in their willingness to lend or to invest, and

(d) the confidence of the clients of the banks, as manifested in their willingness to borrow and use borrowed money.

"The power of a central bank, therefore, to regulate even the money and the capital market is limited, and we must not ask too much of it. We may properly expect it to prevent extreme variations, to moderate the movements in money rates and interest rates, to take up slack at times when rates are unduly low, to meet seasonal needs for increased hand-to-hand currency and seasonal variations in the commercial demands for credit, and, above all, to prevent fantastically high interest rates in times of crisis and emergency. But, under anything like normal conditions, it is quite unreasonable to ask more than this of a central bank."

Only insofar therefore, as the money market is a factor in the price of goods, can a stable money market exert a stabilizing influence on prices. There are many things, however, in addition to the cost of credit or the price of money which enter into the prices of commodities. The ancient economic law of supply and demand cannot be ignored. If both the United States and Canada should produce an abnormally heavy crop of wheat and the United States should produce a very meagre crop of cotton, one would see, other factors on the demand side and the output of other countries remaining the same, low prices for wheat and high prices for cotton, irrespective of any central bank action.

In general, it may be said that a central bank possesses a very limited control over the general commodity price level in a gold standard country. Although it

must be realized that long term variations in the production and consumption of gold have a great deal to do with commodity prices, variations in the production and consumption of goods as well exert a very profound influence and one of much greater significance over the short run.

A disparity in the proportion in which various goods are produced may lead to wide changes both in particular prices and in the general level of commodity prices. To illustrate, an excess production of agricultural commodities, coincident with an inadequate output of manufactured articles, might cause a collapse in agricultural prices so great that the buying power of the agricultural population would be reduced sufficiently that they would be unable even to take the relatively scant output of the manufacturers at prevailing prices, and a decline in the price level of manufactured goods could be expected to result.

CENTRAL BANK INFLUENCE ON GENERAL BUSINESS CONDITIONS

The considerations discussed in the section immediately preceding with respect to commodity prices have considerable application upon investigation into the control possessed by central reserve banking institutions over general business conditions.

In the first place, it must be recognized that the influence of a central bank over the state of trade and industry in general can be effected only through the money and capital markets, an influence which already has been shown to be of subsidiary proportions and of indeterminate degree. Central bank influence can affect only commercial bank credit and this is but one of the main factors influencing the money and capital markets.

Then, too, central banks are operated by men and so long as human nature remains fallible central bank executives may be expected to have definite shortcomings in their diagnosis of business ills and in their prescription of the tonic or surgery necessary to correct the same. Again, a very definite limitation arises because of the non-monetary factors which cause in some degree at least the periodic fluctuations in the level of business. At the present time, the relationship between the monetary and non-monetary factors in the business cycle, their relative importance and interdependence are the subjects of the keenest controversy by the economists of the world. It would seem, however, only logical that where a crisis can be attributed in large measure to causes of other than a

monetary character, the correction of the difficulty might not be possible of achievement by monetary action itself.

In the final analysis, central bank influence over general business conditions probably suffers its greatest limitations as a consequence of the interdependence of nations in the modern economic organization. The importance of international trade, the presence of international financial inter-relationships, and the growth of debtor and creditor positions make it impossible for one country to ignore economic developments in another. Were cooperation always possible between the central banks of the world, this limitation would be of much less significance, but with the nationalistic sentiment so characteristic of the past four or five years the achievement of intelligent and continuous cooperation between the central banking institutions is confronted with very formidable obstacles.

APPLICATION TO CANADA

When attention is directed to Canada, the limitations pointed out possess a special import because of the economic characteristics of the Dominion. Canada presents certain striking peculiarities in its economic organization and financial structure, and these would serve to increase very materially the difficulties inherent in central banking control over commodity prices and business conditions in general.

In the first place, the Dominion possesses no really organized money market. For a central bank that does possess power to bring its influence to bear without violent disturbances to the financial and business structure, it should be operating in a sensitive money market and, if possible, a market which creates bills of exchange in its own currency.

Canada, however, cannot be placed in this category. It does not possess a sensitive money market, it has not yet become a creditor country and probably will not do so for many years. Although it does possess a strong financial structure, that structure is fundamentally simple. Business men discount their bills with the chartered banks of Canada, but there is no market within the country for dealing in bills of exchange nor any organized machinery for carrying out transactions in them, such as exist in London and New York. In general, the Canadian Banks retain the bills which they have discounted to maturity, and probably in the majority of cases such bills will be payable not in Canadian currency but in sterling or in American funds.

Then again, the economic position of Canada as a debtor country and as a country whose major industries are in fields of activity where prices and consumptive demand are ruled by world conditions, would be a powerful deterrent to central banking efforts to control the course of commodity prices or of general business conditions. Professor A. F. W. Plumptre states in this connection:—

> "Countries whose economic system is bound up closely with the export of one or two commodities of highly variable prices and production are clearly not countries whose economic conditions are easily influenced by the volume of money and credit. If harvests are good and world prices are high, attempts to contract bank loans would probably check a boom materially. Nor would efforts to put money into circulation be very effective in alleviating a depression caused by short harvest and low world prices."

CONCLUSION

Upon the basis of the evidence presented, it may be said that it is unlikely that the Bank of Canada will be able to wield a very great influence over the course of commodity prices and general business in Canada, not only because of the limitations confronting central banking action in this regard, but also because of the peculiar character of the economic and financial structure in the Dominion.

The bank might, however, use what statutory and persuasive powers are within its grasp to regulate the flow of foreign capital which is drawn in by and itself aggravates very materially prosperous conditions. Should it be successful in this, the repercussions of a flight of capital in the presence of a heavy burden of debt service payments abroad in depression times might in part at least be avoided. Unquestionably, the Bank of Canada could perform a service of inestimable value to the welfare of the country as a whole by supervising, if not in some degree controlling, Canada's international borrowing and lending.

Lastly, the Bank of Canada can prove of exceptional service to Canadian business by guaranteeing the stability of the monetary standard, protecting its external value, easing off monetary stringencies, preventing the extension of unsound credit in periods of prosperity, guarding the liquidity of the commercial banks and by checking speculative excesses.

RECENT CHANGES IN THE LAW RELATING TO DOMINION COMPANIES

MILLARD J. GRANT

APART from statutory enactment or royal charter, the corporation is a thing unknown to our law, and it is only within comparatively recent years that any general legislation providing for the incorporation of joint-stock companies has existed either in England, whence Canada derives her foundation principles of law, or on this continent. A corporation is a legal entity having the functions of an artificial person and as such is entitled to enjoy the rights and to exercise the privileges of any other person. Legislation with regard to companies has attempted to restrict the manner in which these rights are enjoyed and privileges are exercised, to protect the investors in and others dealing with, the corporation. That such restrictions are essential cannot be doubted when it is remembered that the corporation is an artificial person and, therefore, not subject to corporal punishment and that its assets are limited and may quickly disappear.

Under the British North America Act by which the legislative powers of Parliament and of the Provincial Legislatures are defined, Parliament has been given in addition to a general authority to enact statute law exclusive legislative authority relating to the regulation of trade and commerce, whereas each Province may make laws exclusively with relation to property and civil rights within such Province. Under these powers, Parliament and the Provincial Legislatures have each enacted company statutes. With the large number of security frauds which have taken place within the last few years, it has become evident that company statutes must be more restrictive if the investing public is to be afforded adequate protection. To this end Provincial legislation, applicable to the marketing within the different provinces of securites of any company, has been enacted. These various statutes have accomplished some purpose, but the need for further reform along these lines is very apparent. Parliament has

this year passed a new Companies Act (Statutes of Canada 1934, Chapter 33) which became operative on October 1st, and into which has been carried the existing statute law with the addition of many new requirements relating not only to matters of internal management, but also to the issue and sale of securities which it is hoped may fulfil some of these needs. This Act applies only to companies which apply for and obtain letters patent under it. It has no application to provincially chartered or foreign corporations. If, however, the Act results in creditors and investors being afforded further protection from corporate abuses, it may very well be that it will form a precedent upon which provincial enactments may be modelled.

It is not possible within the limited space of this article to refer in detail to all of the important changes which appear in the new Act, but a few of those of major interest may be dealt with.

Loans to Shareholders

The Act as it formerly stood, absolutely prohibited such loans under any circumstances and saddled the directors and officers assenting thereto with liability to the company for the amount of the loan and interest and to the creditors of the company for all debts of the company then existing or contracted before repayment of the loan. This was a particularly harsh provision in view of the fact that it has become quite the common practice to induce employees to become personally interested in their employer company and some type of financial assistance to this end is in most cases essential. The changed Act permits loans to be made to bona fide employees other than directors with a view to enabling them to purchase shares for their own holding and as well for the purpose of enabling them to purchase or erect dwelling houses for their own use. It also makes provision for private companies to make loans either to shareholders or directors for the purpose of purchasing the stock of an existing, deceased or bankrupt shareholder and thus assists persons originally interested in an enterprise of a private nature in keeping it private. The Directors' liability in the case of the making of a prohibited loan is now limited to the amount of the loan and interest and ceases upon repayment; which is only reasonable and just.

Contracts

Prior to revision, the Act provided that contracts made on behalf of the Company by any agent, officer or servant of the Company

in general accordance with his powers as such under the Company's by-laws, should be binding upon the Company. This has been a source of great disadvantage to persons dealing with an officer who has apparent authority, but who in fact lacks such authority to complete a contract without the prior sanction of his Directors. Outsiders have seldom available to them the private books of the Company and are frequently not in a position to question the authority of the person with whom they are dealing, with the result that they have had to incur certain risks in dealing with corporate agents. As the Act now reads, the contracts made on behalf of the Company by officers or agents acting within the apparent scope of their authority are binding upon the Company which can no longer avail itself of a technical defence to an action for failure to perform.

Changes have also been made in the Law with regard to the filing with the Secretary of State of particulars of mortgages and charges on assets which are not registered under the requirements of various provincial statutes. The former sections in this connection provided that failure to make the required returns of such securities avoided the security as against a Liquidator or Creditor. Failure no longer makes the security void, but only results in certain directors and officers being subject to penalty. Since it is the tendency every year to pass further laws to make it necessary that such mortgages or liens be so registered as to afford any person the opportunity of discovering the condition of the title to the Company's property and assets, it is submitted that this change, although relieving some secured creditors from the danger of loss of their securities, is not in keeping with the general scheme of prohibiting secret liens and charges.

Providing Capital

The first essential to the success of a corporate enterprise, after the preliminaries of organization have been attended to, is to engage sufficient capital for the carrying out of the undertaking and if the company is to expand, it may be frequently necessary to make further offerings of securities. If this capital is to be obtained from sources other than the company's own directorate the stringent provisions of the Act relating to the preparation, filing and delivery of a prospectus must be fully complied with. Heretofore, it was essential only to file with the Secretary of State a document known as a prospectus containing certain formal information regarding the company and its undertaking, or

a similar document known as a statement in lieu of prospectus, but this is no longer sufficient. The word "prospectus" as used in the new Act is so defined as to include every type of graphic communication offering the sale by or for a non-private company, of securities issued or proposed to be issued by it. Every prospectus is required to give under the heading "Statutory Information" certain prescribed details which should enable the cautious investor to judge the merit of the securities for which he is invited to subscribe. It must also contain a full balance sheet duly certified by the auditors of the company, bearing a date not more than four months prior to the date of the prospectus itself. This balance sheet is only required in cases of companies which have operated for more than one year prior to the date of the prospectus, or to new companies which have acquired or are about to acquire established businesses. Other detailed audit information must also be given with statements of opinion as to profits previously made, appraisals, reserves for depreciation and so forth. It is of course impossible to demand such information of new organizations, but, after all, the investment of large amounts of capital is invariably made in enterprises which have had at least one year's operation of which information is available.

Companies are prohibited from accepting any applications for purchase of any of the company's securities offered to the public unless such a prospectus with respect to those very securities has been duly issued, signed and filed and a copy thereof delivered in certain reasonable ways, as provided in the Act, to the applicant at least 24 hours prior to the acceptance of his application. Failure to comply with the provisions requiring this delivery gives the applicant the right to have his application, or the issue and allotment of the securities, rescinded within 30 days of his receipt of notice of allotment or the issue of the securities.

There is now a conclusive presumption that any application, which has been made for securities, has been made upon the faith of the statements contained in the prospectus. This removes the difficulty of an applicant having to prove, in an action for damages or recission on the ground of misstatements contained therein, that he was induced to subscribe by the statements contained in the prospectus alone and not by some other representation made to him at the time of sale. The remedies of an applicant for such misstatements remain substantially the same as before the revision.

The other provisions, however, make it increasingly difficult for those who should be held responsible for misstatements of fact to avail themselves of technical defences.

The Act permits persons selling any corporate securities to communicate with any person who has already received a prospectus. The original invitation to purchase, therefore, may be followed up, but no person acting by or on behalf of the company may call in person at, or communicate by telephone with any residence for this purpose, with the reasonable exception of those of close personal friends, business associates or regular securities customers of that person. Without some such allowance, the provisions relating to the prospectus might result in it being impossible for companies to raise capital at all. This, of course, is not the object of the prospectus provisions. Their purpose is to assure that each investor shall be given the fullest possible information, on the strength of which he may make a decision.

The filing of an old prospectus is not a sufficient compliance with the Act as it now stands. When a prospectus is filed an immediate public offering must be contemplated and must be made bona fide within 30 days of the filing of the prospectus. Otherwise a new one must be prepared and filed. This new provision will assure investors of up-to-date information, and they will no longer have to base their decisions upon statements which may have become obsolete by lapse of time. This is emphasized by the provision requiring the filing of any new material information which may have the effect of altering the prospectus as filed while the securities referred to in the prospectus are being distributed.

The provisions regarding delivery of a prospectus to a security buyer appear to apply only to a direct offer by the Company to the public. They do not apply to cases where the securities have been purchased outright and are being resold by an investment broker. The Act does not assume control over the broker's actions any more than over the actions of any other shareholder in arranging a sale of his securities. Parliament apparently considers that the transactions of these dealers are subject to adequate provincial legislation. The Company, however, in the case of a sale to such a broker, must duly file and deliver to him a prospectus. In this way his customers may gain necessary information of the affairs of the Company by inquiring

through the proper channels. In the past it has been felt that the value of the several provincial securities acts has been lessened by reason of the fact that recognized security houses have had to compete with an army that is engaged constantly in the manufacture and circulation of unsound and plainly fraudulent securities. It is hoped that the new provisions forcing these security issuers to give adequate information may put an end to much of this practise.

IS FINANCIAL ADVERTISING "IN STEP" WITH CHANGED CONDITIONS?

Lorne G. Spry

A PEDDLER stopped abruptly at the front gate confronted by a ferocious dog that barked loudly. "Come right in," said the lady of the house, "Prince barks a lot but he won't bite you." To which the peddler replied: "You may know that, madam, and I may know it . . . but does the dog know it?"

The main reason why the written contacts of financial institutions with the public are not more human and understandable is a decided lack of knowledge of what the public already knows and what it does not know about financial institutions and financial transactions.

During the past ten to twenty years, financial advertising has been vastly more human. The "starch" or stiffness has been removed but for some reason the "spinach" has not been put in.

Harrison Jones, Executive Vice-President of the Coca Cola Company, one of the North American Continent's outstanding and highly successful advertisers, was invited to address the recent annual convention of the Financial Advertisers Association on the subject: "What does the average man ask about his bank?"

"The bank," he said, "is a necessary part of our economic life. Why not say so? It is an adjunct to every individual and every firm. Why not say so? It serves a definite utility and makes a definite contribution. Why not say so? It renders a service fairly and honourably, and charges for its service a fair profit, which is no different from any other business transaction. Why not say so? There is no *legerdemain*—there is no secret art; there is no chicanery; there is no sinister manipulation among honourable bankers and in

honourable banking. Why not say so? I think the time has come to practice self-revelation; to take the audience, who have sat agog, mystified and perturbed at our performance, behind the scenes and show them the inside workings of one of the world's greatest businesses. This cannot be done in a day, nor in a year. It cannot be done spasmodically, and it cannot be done by one institution. One hundred and twenty millions of people must be reached. They must be reached constantly, continuously and consistently. Every little phase of the banking business that you may desire to make known must be told a dozen times and in a dozen different ways and illustrated in every conceivable way. It seems to me there is an opportunity for a joint action, or joint campaign, national in scope, of several years' duration, to set this business before the eyes of the public and turn on the lime-light—for you have a story to tell, you have a product to sell, and 'IF YOU'RE GOING TO SELL 'EM, YOU GOTTA TELL 'EM!'"

Men who are given the responsibility of preparing financial advertising are beginning to learn that the best way to find what the public knows, and does not know, is to get out and ask. They realize that this is a technique commonly used in merchandising groceries, shoes, and practically every other commodity . . . . yet it has been sadly neglected in selling the services of financial institutions. Unfortunately, too many financial campaigns have been prepared from officials' viewpoint instead of the public's viewpoint; and the two rarely gibe because too frequently those on the inside are unfamiliar with what the public knows and does not know about financial transactions and services.

"Advertising, spoken or written, is explanation for mutual profit" but financial advertising managers, in times of general dilemma, are obliged to consider situations such as these:

—savings institutions tussling with questions of interest rates and seeking profitable avenues of investment for deposits;

—commercial banks, mortgage and trust corporations struggling with service charges on deposit accounts that have become unprofitable, in consequence of too generous use and abuse of chequing privileges;

—trust companies striving to conserve estates and maintain income for beneficiaries while coping with such competition as is offered by life insurance company deposits and annuities;

—investment companies trying

to carry on under the greater restrictions imposed by the Securities Act;

—and finally, financial advertising departments trying to work out effective sales programmes under these conditions and more particularly under the bankers' own taboos, inspired by the introduction of unjust legislation which, in many instances, is undermining the very foundation of sound finance and the sacred regard for covenants.

These problems are not peculiar to any one institution. They are with all of us and they need the application of tolerance working through employees, customers, the public and the press.

Fred N. Shepherd, Executive Manager of the American Bankers Association, recently threw out to financial advertising men a vigorous challenge to bring about a better understanding between bankers and the public. "Out of present conditions and events of the past few years there comes to you an unmistakable mandate," he declared. "It challenges you to help bring about between the banker and the people a greater degree of understanding, a clearer vision of mutual interest and a larger measure of common knowledge regarding banking realities than has ever before existed.

"Among the causes of our banking troubles," he added, "was the fact that millions of our people have been taught not how to USE banks, but how to MISUSE them.

"It is your opportunity through your customer advertising material and your customer contact policies," Mr. Shepherd continued, "to imbue the minds of those who come into your institutions with fundamentally right conceptions as to what a bank can and should do for them and what obligations they can and must observe toward the bank.

"Simply to get customers is not enough. It is essential to get customers in the right frame of mind.

"You also have a broader opportunity," Mr. Shepherd continued, "through advertising in the public prints, to impress upon the general public an understanding of the social and economic function which banking institutions can and do perform. It is not sufficient that you sell your own bank to your immediate public with an eye single to its own growth. You may also build up, bank by bank, strong defenses for all true banking against popular misconceptions, political misrepresentation and subversive interference."

Mr. Shepherd denounced the practice of paying for deposits with such services as the maintenance of day nurseries, acting as

railroad ticket agents, collecting fraternal dues, distributing baseball bats and balls, distributing Christmas baskets, seeds, calendars, trinkets and all sorts of gadgets, issuing cashier's cheques at par for payment of non-customers' local bills, specially printed cheque books, free credit information, overdrafts, drawings against uncollected funds, armored car service, making up of payrolls, etc.

"In 1929, the American Bankers Association Commission on Banking Practices and Clearing House Functions estimated that banks were spending over $5,000,000 annually above any revenue which might be derived from giving things away and that free services were costing banks more than $300,000,000 a year," Mr Shepherd stated.

"These practices," he declared, "probably did more harm in respect to creating misunderstanding in the public mind as to what was really to be expected from a bank than they did in respect to operating costs.

"The people simply did not take banking seriously enough; we must not only get and hold business but we must get and hold it by proper methods.

"We must develop in the minds of those who use banks, or of those who think about banks, a proper conception of what a bank is and what it should do, instead of leading them to expect all manner of doubtful services."

Turning to the question of what banks should offer the public, Mr. Shepherd asserted that the physical facilities of the banks, their experience, legal requirements and other safeguards, the financial arrangements connected with the interchange of the community's products and services, the paying of its multitudinous bills, the accumulation of its savings and the loaning of money to its constructive business enterprises and for its public requirements constitute the major returns which banks give their depositors for the privilege of loaning and investing their money at a profit.

"When a citizen in a bank's community places his funds on deposit, is it not true that the increased mobility and economy which banking facilities give his money substantially enhance its real value to him because of its increased utility?" he asked.

"Is it not true that the highly developed technical equipment, scientific methods and inter-bank co-operative relationships existing in the American banking system enable it to perform these services and many others with the maximum of efficiency and minimum of cost?

"And is it not true that honestly

and skilfully managed banking through employing these funds profitably for itself and at the same time so as to defray the cost of the banking mechanism to the public, renders the people economic services obtainable through no other channels?

"Properly told messages embodying this philosophy of banking constitute the best sales argument not only to get customers into the bank but to get them into the bank in the right frame of mind," Mr. Shepherd declared.

"If extensively used," he added, "such copy should serve the welfare of all banking in creating sounder public understanding of the proper functions of banking and the bank's place in the nation's life."

Is financial advertising "in step" with changed conditions? To advertise for saving deposits, investments and trust business is one thing, but the important thing for the advertising manager to consider, ahead of time, is whether the business resulting from his institution's advertising can be profitably handled. In this discussion of financial advertising we have attempted to show what the financial advertiser must know rather than what has been accomplished through advertising on the part of Canadian financial institutions in recent years. References have been made to authorities on this subject in the United States of America who at last are making an honest effort to meet the public's demand for financial information. W. C. Clark, our own Deputy Minister of Finance, who was guest speaker at the recent convention of the Financial Advertisers Association, said: "Although your problem was more difficult than ours because of the difficulties of your banking system a year or more ago, yet there should be much that each can learn from the other's experience."

Canada's financial institutions, with a background of British traditions and conservative policies, have weathered the economic storm. In the nation to the south of us financial institutions appear to be putting their houses in order.

CANADIAN SECURITIES PUBLICLY OFFERED IN THE UNITED STATES

FERDINAND C. CARSON

AS a result of the geographic proximity of the two countries and of the fact that most of the social and economic institutions of both were transplanted from Great Britain and modified to fit conditions peculiar to the respective countries, Canadian securities have played a prominent role in the capital market of the United States. While it can scarcely be said that no distinction whatsoever has been made between Canadian and domestic securities it is true that Canadians are usually considered as constituting a class distinct from the "foreign" group.

The United States was an importer of capital until the outbreak of the world war, but was also an exporter of small amounts of capital during the twenty year period immediately preceding the war. During the course of the war the major portion of United States securities held abroad were repatriated and in addition, large sums were loaned abroad. This outflow of funds on a large scale continued after the war and at the present time the United States is a creditor on the long-term capital account to the extent of about 14 billion dollars, exclusive of intergovernmental debts, which amount to more than 12 billion dollars.

During the entire period of United States foreign lending, Canadian governments, national, provincial and municipal, and Canadian corporations have obtained large sums in New York and other financial centers by publicly offering their securities. Still larger sums of American capital have been invested directly in Canadian enterprises, including American owned factories in Canada and shares and bonds of Canadian corporations purchased in the Canadian securities markets. Further, during the course of the past year when United States capital was "fleeing from the dollar" substantial amounts were transferred to Canada.

U. S. Has 29% of Foreign Investments in Canada

As of December 31, 1933, the total foreign investments of the United States were estimated by the Department of Commerce at $13,800,000,000 of which $3,950,-000,000 or about 29 per cent. represented investments in Canada. The amount invested in Canada was more than three times as large as that invested in any other single country. Of the total invested in Canada, $1,880,000,000 represent portfolio investments and $2,070,000,000 direct investments.

The Canadian portfolio investments have emerged practically unscathed from the wave of bond defaults which began in 1931. According to a study of dollar bonds in default published by the Institute of International Finance of New York on May 14, 1934, Candian dollar bonds in default on March 1, 1934, amounted to only $137,396,900 or 7.3 per cent. of the total portfolio investments. On the same date 37.6 per cent. of the total foreign bonds held in the United States were in default. With the exception of a $400,000 obligation of the City of St. Boniface all of the bonds in default are obligations of corporations. Of the $136,996,900 of corporate obligations in default, a substantial portion has been adjusted or is now in the process of being adjusted. For example, Abitibi Power & Paper Co., which defaulted on the $48,267,000 of its 5's of 1928-53 is in receivership and will, no doubt, be reorganized; a payment of $70.00 per $100.00 bond has been made on the $20,000,000 of Ontario Power Service Corp., Ltd., 5½'s of 1930-60.

Earnings on direct investments are more difficult to ascertain, but it has been estimated that the total net income on this type of investment in Canada amounted to between 1.75 per cent. and 2.75 per cent. of the total, as compared with profits of between 1.13 per cent. and 1.5 per cent. on direct investments in Europe and with profits of between 2.9 per cent. and 4.2 per cent. on direct investments in Latin America.

Canadian Security Record is Relatively Good

This record of performance by Canadian securities, especially portfolio investments, is enviable as compared on any basis with securities of United States entities and is particularly enviable when compared with securities of other foreign countries.

As stated above, the same distinction has not been made between domestic and Canadian securities as has been made between domestic and foreign securities other than Canadian. Under the Securities Act of 1933, passed by the Seventy-Third Congress, how-

ever, the line of distinction is drawn more clearly, especially as regards government and political subdivisional securities. All issues of domestic corporations except, in general, those which are under Federal Government supervision and all foreign issues, government and corporate, must be registered with the Securities and Exchange Commission prior to the offering of the securities. Registration is not required in the case of United States government and political subdivisions.

Security underwriters have severely criticized the Securities Act, contending that the regulations are too strict and that the reluctance of underwriters and of issuers to assume liability and responsibility in accordance with the Act is delaying the flotation of new issues and thereby retarding recovery. Since all foreign securities must be registered before issuance, Canadian governing bodies and corporations will be affected in the same way as United States corporations are affected. While it is true that there has been a dearth of new security issues in the United States in the past year, the same situation has prevailed in England. During the first six months of 1934 new securities sold in the United States, exclusive of those of the Federal Government and of refunding issues, amounted to $604,000,000 as compared with about £70,0000,000 or $350,000,000 issued in England, exclusive of British Government and refunding issues. The issuance of corporate securities only is regulated in England and such regulation is not new in the English capital market.

Lack of Demand for Capital by Business Means More Financing by Governments in Canada

While the strict regulation which has been imposed by the United States Government may be in part responsible for the lack of new issues in the capital market of the United States, the lack of demand for new capital is of much greater importance. New issues of railroad securities, which are specifically exempt from the provisions of the Securities Act, have been conspicuously lacking during the past two years. Corporations do not need new capital for expansion under present circumstances and since corporate shares and bonds comprise by far the major portion of securities in any capital market, the total of new capital obtained in the various markets has shown a marked decline during the past three years. Canada has in the past supplied an increasing proportion of its own capital requirements. Higher returns are paid by business than by governments

and for this reason the available Canadian capital has, until recently, been absorbed largely by Canadian business enterprises. As a result of the absorption of the Canadian investment funds by business, the national and local governments were either forced to borrow abroad, or pay a much higher rate for funds at home than was called for by their credit standing. During the past two or three years, however, business has not needed new capital, as a result of which the Canadian governing bodies have been able to borrow practically all the funds they have required in the domestic market.

As soon, however, as Canadian corporations reappear as takers of capital, thereby causing an upward movement in interest rates, the public bodies will reappear as borrowers in the international capital markets. Canadian corporations may also find it desirable to obtain part of their capital abroad. And if due recognition is given to the past performance of Canadian securities by United States investors, new Canadian issues should find a ready market in the United States.

CURRENT EVENTS

ARTHUR G. DORLAND, PH.D.

Recent Political Assassinations

THE past summer since this publication went to press, has not lacked spectacular incidents. Most striking of all are the shocking political assassinations that have occurred during the last few months, representing only a small proportion of similar episodes of the past two years. Mention of only a few that have occurred within this period may serve to bring this fact home:—The assassination of President Doumer, of France, May, 1932; of Mr. Inukai, Premier of Japan, May, 1932; of Colonel Sanchez Cerro, President of Peru, April, 1933; of the King of Afghanistan, November, 1933; of Colonel Pieracki, Polish Minister of the Interior, June, 1934; in the same month the political murder of Ernst Roehm, Commander of the German Storm Troops, and several of his colleagues; the assassination of Doctor Dollfuss, Chancellor of Austria, July, 1934; and now this double tragedy of October, 1934, the assassination of M. Louis Barthou, Foreign Minister of France, and of King Alexander of Jugo-Slavia at Marseilles.

The Tragedy of Austria

The last two tragedies of this fateful year have probably excited the most interest and comment. The late Austrian Chancellor, Doctor Dollfuss, was a well-known figure who despite his diminutive person possessed great qualities of energy, determination and personal charm that caught the imagination of the outside world. A gallant little figure but a pathetic one, fighting a losing battle with weapons of doubtful value, and facing a very difficult situation made still more difficult by his tactical errors.

Instead of seeking to unite under Democratic Liberal institutions the little that was left of Austria, Dollfuss determined at the behest of the Vatican and Italian Fascism to destroy the Austrian Social Democratic party, and thereby incurred the bitter enmity of this important group. Surely this was a mistake, since the Social Demo-

crats would be the strongest ally of any Liberal Government and also the natural enemy of the German Nazi Movement which was the most serious threat to Austrian independence. This tactical error in turn, compelled Dollfuss to lean more heavily than ever on Italian Fascist support, thereby increasing his difficulties by bringing into the Nazi camp thousands who would have stayed outside if he had tried to form a United Democratic front with Socialists backing. The impartial observer is left to conclude that the path he followed of reaction and repression, Clericalism and Fascism has offered no solution to Austria's dilemma, and its latter state is worse than the first.

Some History Behind the Assassination of King Alexander

To those who know something about the troubled history of Jugo-Slavia the assassination of King Alexander has not come as any surprise. His family attained its present position by assassination and intrigue, and for years Alexander has maintained his rule only by methods of violence and terrorism.

The family of the late King of Jugo-Slavia was closely connected with Serbian problems which contributed to the immediate causes of the Great War. The father of the late King, Peter I, was associated with the Palace Revolution of 1903 which caused the brutal murder of the ruling King Alexander and his Consort, Queen Draga, representative of the Obrenovich family which was traditionally friendly to Austria, and placed in his stead the usurping Peter I., a representative of the rival family of Kara George Petrovich, who now reversed the policy of Serbia by placing her under the leadership of Russia to become the spear head of Russian expansion in the Balkans. Confident in the knowledge of Russian support, Serbia pursued its policy of nationalistic expansion, aiming to secure from Austria the former Turkish provinces of Bosnia and Herzegovina and to assume hegemony over all the south Slavs within the Austrian Empire of that day. Such an ambitious and aggressive policy was possible only with Russian and French backing, since it aimed at nothing less than the destruction of the old Austrian Empire which at that time contained more Slavs than Germans and Hungarians combined. Resistance to Serbian nationalistic aims backed by Russia and France, naturally became the corner-stone of Austrian foreign policy; and it was regarded by her as a purely

defensive measure to safeguard her very existence.

The murder of the heir to the Austrian throne and his wife on Austrian territory in June, 1914, by assassins who were provided with arms and bombs by a notorious Serbian secret nationalistic society that included among its members important officials in the Serbian army and intelligence staff, was naturally felt by Austria to be sufficient provocation for strong retaliatory measures. The interference on behalf of Serbia by Russia and France, backed by England, and the support of Austrian policy rashly promised in advance by Germany, made it impossible to isolate the issue as a Balkan problem, and accordingly precipitated a general European war between the two rival groups of powers.

One important result of the Great War was the breakup of the Austrian empire into a number of succession states, among them being the new Kingdom of the Serbs, Croats and Slovenes—as it was at first known—under the leadership of the late King Alexander of Jugo-Slavia. The Croats, however, have never been satisfied with their status in the new kingdom. They favoured a federal state in which they would retain large powers of self-government, rather than the highly centralised state under Serbian domination which the Jugo-Slav constitution of 1921 imposed upon them. A strong Croatian peasant party now developed under the leadership of Stepan Raditch who was violently opposed by the government or the nationalist party. In 1928 government supporters fired upon leaders and members of the Croatian Parliamentary Party killing and wounding several, among them being Stepan Raditch who later died from the effects of his wounds. In 1929 the continued opposition of the Croatian element finally induced King Alexander to dissolve parliament and to abrogate the constitution of 1921, thereby transforming the Kingdom into an absolute monarchy under the king who assumed complete and sole authority over every office of the state. Severe restrictions were placed upon the press, penalties were enforced for criticising or resisting measures of the dictatorship, the carrying of arms was forbidden, and all political gatherings were prohibited unless authorized by the police. Three years ago this September, King Alexander announced that the dictatorship was at an end, and a new constitution was introduced. The new forms of government were manipulated in such a way, however, as to retain power in the hands of the old Nationalist Party, and con-

sequently failed to conciliate the Croats who continued their policy of resisting the Serbization of the government and of the people.

King Alexander knew that he had made countless enemies by his repressive policy, and remembering the 1903 regicide and the assassination of Stepan Raditch, he had for a long time feared a similar violent death and surrounded himself by the most elaborate precautions for his safety. Whether the arrangements made to protect him by the French police during his diplomatic visit to France were competent or not, probably made little difference to his ultimate fate, since he had been a marked man for many years. Four previous attempts had already been made on his life. The last attempt was made last March when three men attempted to shoot him during his visit to Zagreb, the Croat capital. The three would-be assassins were all executed. His unfortunate young son has inherited a legacy of troubles that would daunt the ablest and most courageous leader; and it is a nice question whether monarchy will be able to maintain itself at all in Jugo-Slavia, which might in the near future revert to some form of Republican government.

Some Hopeful Features in the Balkan Situation

The disturbed condition of Jugo-Slavia to-day does not, however, present the same threat to peace as in 1914, when the shot fired by a Bosnian assassin was the spark which set the world alight. The ill feeling between Italy and Jugo-Slavia that has kept Europe on tenter-hooks has been largely the result of a press campaign of villification conducted by both sides, that is officially inspired because it serves the purpose of the dictatorial governments in both countries to divert public criticism from themselves by attacking the good faith and intentions of their neighbours. Neither Italy nor Jugo-Slavia really want war, but rattling the sabre has its uses for domestic consumption and is a well-known device.

Another reason for regarding the present Balkan situation as less dangerous than in pre-war days is the fact that the Great Powers of to-day have different policies in relation to the Balkans; while the Balkan states themselves have become more conscious of their common interests and are less amenable to external influences than they formerly were. A significant illustration of this tendency is the Balkan Entente signed early in 1934, the main object of which

being to warn off the Great Powers from interference in Balkan affairs. For it is worthwhile to remember that the sinister expression 'balkanisation' derived its meaning, not from Balkan disunity but from the rival greed of the Great Powers in exploiting it. The Balkan states can prevent this by recognising their common interests and refusing to be mere pawns on the international chess board as they were largely in the past.

The Admission of Russia to the League

The admission of Russia to the League of Nations is a rather more cheering incident to record. The withdrawal of Japan and Germany from the League was a serious blow to its prestige which the recent addition of Russia will help to restore. Russia is by no means *persona grata* to many of the League members. Switzerland, Belgium, Holland, Hungary and some Latin American countries—to mention only a few—were inclined to object; but these objections were not sufficiently numerous to prevent Russia's admission which Great Britain, France and Italy for various reasons were disposed to favour.

The extent of Russia and her vast rapidly developing resources make her co-operation with the League a desirable and tremendously important though unpredictable factor. But who can affirm that Russia may not make a worthy contribution to world peace? For it may be recalled that in the past Russia has had an important part in the history of European peace movements. It was Czar Alexander who was the most prominent figure in the settlement of Europe after the Revolutionary and Napoleonic Wars, and who promulgated the famous Holy Alliance as a means of promoting peace among the great powers of that day. A later Czar of Russia was responsible for calling the Hague Conference of 1889—the first concerted attempt to establish a world order based on disarmament and on impartial arbitrament of disputes. Many of these ideals may still be far from attainment; but Russia has an historic association with some of the earliest essays in this direction, and her affiliation with the League is a good omen for the future.

Russia's present Communist ideals more than anything else are the main reason for her unpopularity. But some time ago Russia announced her willingness to abandon subversive Communist propaganda, and since that time there is no evidence of bad faith in the keeping of this promise. In any case with Russia now a member of the League, a breach of this understanding would make the

protest of any aggrieved country all the more effective. One good effect of Russia's entry into the League is already apparent in a marked lessening of the dangerous tension between Russia and Japan in the Far East.

The International Labour Organization Advances

Closely associated with the League and representing another important link in the, of late, rather fragile chain of world co-operation is the official acceptance by the United States government of the invitation to become a member of the International Labour Organization—a step which roused enthusiasm in labour circles the world over. The United States will at last be in a position to lend its full support to the great labour movements centring in Geneva to raise the labour of all nations to proper living standards. Such incidents, though unattended by the blare of trumpets and too often unnoticed by the Press, are among the hopeful signs of the time, that the foundations of world co-operation are being gradually established. Certainly there is much essential spade work still to be done in the economic and social fields of international relations, before any great betterment in the sphere of political relations will become evident.

WAGE POLICIES IN CANADIAN INDUSTRY

From the Thesis of the Same Title

STEWART N. STEVENS

PEOPLE who have given even superficial study to the subject of wage payment plans are beginning to realize the enormous gain that can be made in the efficiency of workmen if they are properly directed and provided with suitable appliances. Few, however, have realized another fact of equal importance, namely that to maintain permanently this increase in efficiency, the workman must be allowed a portion of the benefit derived from it.

To obtain this high degree of efficiency successfully, the same careful scientific analysis and investigation must be applied to every labour detail that the chemist or biologist applies to his work. Whenever this has been done, it has been found possible to reduce expenses and, at the same time, to increase wages, producing a condition satisfactory to both employer and employee.

The great difficulty in instituting this method of dealing with labour questions is that usually neither employer nor employee has sufficient knowledge of the scientific method to realize either the amount of detail work necessary, or the extent of the benefits to be derived from it. In general, their inclination is to adhere to the methods with which they are familiar, even though these methods have failed to bring them appreciably nearer the solution of their problems, and to distrust all others, although newer plans have produced results far more satisfactory than they even hoped for. A scientific investigation into the details of a condition that has grown up unassisted by science has never yet failed to show that economies and improve-

ments are feasible, that benefit both parties to an extent unsuspected by either.

The purpose of this study was to determine, if possible, just how far Canadian manufacturers have gone in this matter of scientific investigation into the relations between employer and employee. There are leaders in everything, no matter what it is, and so there must be pioneers in the field of scientific management. The problem was to discover who these leaders were and whether or not their results were up to expectations; whether scientific methods have spread across the country and into every type of industry, or whether only a few have so far adapted themselves to the new methods. To make the investigation complete it was found advisable to study all types of wage policies and report on the extent of use of each, and, at the same time, to find out whether or not they are operating successfully.

In order to obtain this information, one hundred and seventy-five letters were sent out to representative companies in twelve of the leading industries of Canada. Enclosed with each letter was a questionnaire which the executives of the companies were asked to fill out and return. It was also suggested in the letters that any additional comments on wage policies would be welcomed. These letters were sent to companies across the whole country from Halifax to Vancouver so that the replies would be representative of the country as a whole and not one particular section. In picking the mailing list also, every effort was made to choose companies of various size so that any differences would be noted. Only a few questions were asked as it was thought the simpler the questionnaire the higher would be the percentage of replies. The questionnaire was, nevertheless, made as complete as possible in order to get the maximum of information.

The results of the questionnaire were very satisfactory. From the one hundred and seventy-five letters sent out, there were approximately eighty replies, which is about forty-five per cent. These replies came from every industry on the list, and while the majority came from Eastern Canada, yet enough of them were from the West to act as a check. Most companies were content to fill in the questionnaire and enclose it with a short personal letter, but a few went into detail concerning their systems and these replies were extremely helpful. The results were classified according to industry, and then reclassified according to the type of payment plan used. In this way it was possible

to tell at a glance the number of companies in each industry which had made investigations along the lines of scientific management. Some of these replies were checked with information from the Department of Labour at Ottawa and found to be essentially correct. So while the result may not have been perfect in all its details, yet it is on the whole correct and should give a fair idea of the types of wage policies used in Canadian industry and just how far scientific management has progressed. The discussion will be divided into three divisions: day wage plans, piece work plans, and wage incentives.

Day Wage Payment Plans

Under the day wage method of payment, the employee is paid a certain rate per hour for each hour during which he is at work in the shop. There is no direct connection between the rate of production on any given job and the pay which he receives, although there may be some indirect connection, inasmuch as the better workman usually has a higher rate of pay.

The answers received from the Canadian manufacturers, in reply to the questionnaire sent to them, show, naturally, a wide variation. Their replies, which have been divided into different industrial classifications, show beyond the shadow of a doubt, that day wages are more effective in some industries than in others. For instance, in the iron and steel industry day wages are used only for non-productive workers. Wherever possible, these companies have installed incentive plans of one form or another in the belief that they result in greater efficiency.

The replies received from the pulp and paper industry indicate that day wages are quite widely used. The reason for the use of day wages in this industry is found in the reply of one of the companies. It stated that most newsprint mills are union mills with a scale of hourly wage rates. Another reason for the day wages is that there is not quite as much standardization in this industry and employees make use of their own initiative to a greater extent.

Two flour milling companies reported that day wages are widely used in that industry, because the manufacture of flour is largely mechanical requiring very few trained men. It seems that if the job does not require a great deal of skill, day wages are a satisfactory method of payment. On the other hand, companies engaged in the manufacture of rubber products report that day wages are entirely unsuitable, because their plants need skilled workers and

their operations have been standardized to a great extent. None of them feel that the day wage method offers sufficient inducement to keep up the rate of production.

When the industries in question are briefly reviewed, it is found that the pulp and paper, oil refining, beverage, milling and agricultural implement industries definitely favour day rates in the majority of cases. The chief reasons as brought out in their letters seem to be that highly skilled workers are not needed, that the work is such as to make simplification and standardization extremely difficult, and finally, there is the difficulty of keeping the wages of the workers on an equitable basis if a bonus system is used.

As a conclusion to the discussion on day wages, it may be said that the type of industry is of prime importance in determining the wage policy, as some are suited for incentives while others are more successful under day wage payments. Additional information gleaned from the replies indicates that while very small plants have to use day, being equipped for no other, yet beyond that, size means little, as some of the largest companies use day wages exclusively. The location of the plant exerts some influence on the wage policy, since some workers are by nature against incentives while others prefer day wages because they are the only ones they know and understand. In the larger centres this opposition is not encountered. Day wages on the whole, seem to have a permanent place in industry, but gradually scientific management is substituting newer and more economical methods.

Piece Wage Payment Plans

The second of the older plans of paying workers is to fix a price for the completion of a given task, and pay that price without reference to the time taken in completing the task. The task may be either the completion of one unit or of a given amount of work, and the rate is ordinarily termed a piece rate.

It seems obvious that the important factor in a successful piece wage system is the proper setting of the rate. When piece rates were first introduced, the rate was usually reached by means of an intelligent guess and a bit of experimentation. This meant an unfair wage to some and resulting discontent. At the present time, rates are set very carefully and in as scientific a manner as possible.

According to the replies received from the questionnaire, piece rates are quite popular in Canadian industry. Wherever the work is so standardized that piece rates are

practical, they are usually in operation. Steel manufacturing plants, for instance, seem to favour the use of piece rates in their plants. The personnel manager of a large company of this type, with factories in all sections of Canada, writes as follows: "Other than in our warehousing, shipping, inspection, planning and supervising work, the majority of our factory employees are paid by piece work. Our main policy is to have all production work paid from piece work rates set after a fair time study has been made. The operator is advised of that rate. The plan is simple and direct, is easily understood, and leaves no cause for dispute or disappointment when pay day arrives."

The textile industry has an ideal arrangement for the use of piece rates, according to the replies received. Out of a total of nine replies, eight make use of piece rates to pay the majority of their men. Only the indirect workers are paid day wages, and one of the companies is searching for a way by means of which even these indirect, non-productive workers might be placed on the same basis as the rest of the payroll. In these factories, machinery plays an important part in production, as most of the processes are repeated over and over again. The operator of the machine becomes very expert at this one operation and is able to speed up his production considerably if he is offered an incentive for so doing. Piece rates provide this necessary incentive.

A similar situation exists in the boot and shoe industry. The six companies which replied to the questionnaire all use piece rates to some extent, and they seem to feel that this method of payment is the most satisfactory. Machines play an important part in the manufacturing processes and operations are so standardized that the operators of the machines are able to earn more through the use of piece rates, provided, of course, the rates are set in an equitable manner.

Most of the companies using piece rates seem to have fairly large plants but this need not necessarily be the case. According to "Factory and Industrial Management", September, 1932, page 342, it is just as possible for small concerns to be scientifically managed as large ones. An investigator in scientific management found years ago that there are only seventeen different hand motions, and they are repeated millions of times daily in small industries just as in large. Workers in small industries walk and stoop and lift and pull and push just the same as in large industries, perhaps not always in a fixed order or sequence, which

might make the problem a little more complicated, but not more fundamentally different.

Thus, while up to the present, piece rates have been used more in the medium and larger Canadian concerns, yet it seems possible that the near future will see a spreading of the system to the smaller plants. This development may quite possibly be accentuated by the present depression which has certainly done much to focus the attention of executives upon the need for scientific management. Piece rates can be as effective a method of payment as any, if they are administered in a scientific and equitable manner.

Wage Incentives

Most workers are conscientious and wish to produce a normal, fair day's work in return for the wages they receive, just as much as management expects a fair day's work for which it is paying. Few men resent working to a fair standard when they know extra performance means extra compensation, and vice versa. In forming a sound wage incentive plan for a particular company, it is important to remember that the engineer is more important than the plan. A poor plan in the hands of a good engineer is a better combination than a good plan in the hands of an incompetent man.

This is not the occasion for a detailed study of the many different methods of awarding a premium or bonus. The common feature of them all is that they set a specified quantity of work as a standard task and then give the worker an additional reward for doing better than the task. Some of the better known and more widely used premium plans are the Taylor Differential Piece Rate, Gantt Task and Bonus Plan, Bedaux Point System and the various group bonus systems. There are several other types and individual variations of wage incentive, but these few are the ones most widely used in Canada, as far as can be determined.

In the questionnaire sent out to Canadian manufacturers, the first interesting point was found to be that Canadian industry has not yet adopted incentive plans to the same extent as the United States. They seem to feel that their plants are not adapted to this form of payment and find straight piece rates or hourly rates quite satisfactory for their purposes.

But it is significant to note that those firms reporting the use of incentives are unanimously in favour of them and claim they are vastly superior to other forms. There is, however, one thing which must be remembered. Very few

companies are willing publicly to condemn their own policy, and consequently are quite likely to overlook faults in filling out a questionnaire. So the results of any such investigation as this should be weighted to allow for over-enthusiasm. It is obvious, nevertheless, that many Canadian manufacturers have experimented with premium plans and found them successful.

Some of the larger Canadian textile mills are beginning to experiment with bonus systems. While most of the companies in this industry operate on piece rates, the general superintendent of a large mill which is considering the adoption of a wage incentive plan, made the following statement: "While we do not wish to favour any one system, we believe that errors in selection are often made through lack of proper consideration for how existing conditions in the plant correspond to the results which are desired. By this we mean that a certain state of efficiency and physical fitness is necessary in preparation for a premium system of wage payment as well as recognition by the management, of the mutual benefits possible through improved cooperation and morale, provided the premium distribution is reasonable and worthy of the effort."

The rubber industry has, perhaps, gone further than any other industry in Canada in the installation of wage incentive plans. Replies were received from five of the largest producers in Canada, and of these four have installed premium plans while the fifth has a scientifically managed piece work system. In this connection it is significant to note that many of the large companies in this industry are branches of American concerns, which might account, in a large measure, for the adoption of the systems here. The primary iron and steel producers also make use of production bonuses to some extent, while the newsprint and electrical equipment manufacturers as well as the large automobile producers are experimenting in this direction, and some successful installations have been made. It is, however, very hard to persuade the producers to get out of their present rut, and experiment with these new systems. Many executives feel that they would rather not take the chance of disrupting the present friendly relations with their employees and so they keep on in the same old way.

It is further noticed that the companies using these incentive plans are practically all large producers. The smaller plants have not made much use of bonuses because they feel they can keep a sufficient check on their employees

without going to all the expense necessary to install one of these systems. It must be admitted that incentives are not nearly as necessary in very small plants where supervision can keep adequate control over the employees. As mentioned before, there is no real reason why scientific management cannot just as well be applied to small plants as to large ones, yet it would be foolish for a small producer to go to a great expense to install a complete wage incentive plan when the same results can be obtained without it. So it seems likely that the use of scientifically administered incentive systems will be confined to the larger producers for the next few years.

In selecting the perfect wage payment plan, the most important thing to remember is that whatever plan is chosen must be adapted to individual environment. A plan which may prove successful in one factory may be a failure in another factory in a similar industry, simply because of the failure to take into account surroundings, both in factory and home.

Another important point to remember is that any plan well carried out may produce better results than a better plan not so well carried out. Therefore, it can probably be said that the execution of any wage system is at least as important as the system itself.

That system of wage payment should be best which will result in the lowest costs at a given wage, or the highest wage for a given cost. The first requirement is to encourage every man's best efforts. The problem is to do this at the least expense in order that the largest possible part of the cost may go directly to him and not be dissipated in expense of administering the plan.

If any conclusions at all can be drawn from this study, the most important one would seem to be that scientific wage incentives, (well-managed piece work and premium plans) have certain definite advantages over the old-fashioned day wages. While far from all of the industrial concerns in Canada have installed incentives, yet the trend is in that direction and at least one or two companies in almost every industry are experimenting with them. These companies honestly believe that they can not only decrease costs and increase output, but that they can help the workmen by paying increased wages. There is reason to believe that incentive wage policies can go a long way toward healing the breach which has, for so long, separated the employer and his workmen. As the employees come to understand the system better, they too will realize its advantages. But, as mentioned before,

local conditions are of prime importance and no change should be considered until extensive preparations have been made, and management is certain the workers understand and appreciate what is being done. If these conditions are observed there is every reason to suppose that both Canadian manufacturers and Canadian workmen will be better satisfied in the years to come.

A SURVEY OF PRESENT RETAIL CREDIT PRACTICES

Condensed by Brock Short from the Thesis "Commercial Credit"

By ROBERT R. GLOVER

RETAIL stores, in their attempts to make it easy for the customer to buy, and by their offer of credit extension, bring a certain number of grave problems upon themselves.

The first decision that must be made by retail stores is whether the store will grant credit or whether sales will be strictly for cash. If a store decides to grant credit, it is imperative that a definite policy be formulated so that all credit requests may be treated with uniformity.

A survey of actual retail credit practices in Canada brings to light a great variety of policies.[1] The investigation was carried out by means of personal interviews and the number of firms studied was sufficient in every case to insure a representative result. The interviews covered every phase of credit business; the volume, the capital involved, the bad debts, the firm's policy, the investigations made, *et cetera*. This is indicative of the wide divergence of opinion concerning credit among business men.

The survey showed that 65 per cent. of the merchants follow a supervised credit policy, 10 per cent. follow a very free policy, and 25 per cent. have no consistent policy whatever.

An Inconsistent Policy on Credit is Relatively Satisfactory

The inconsistent theory on giving credit is based on the supposition that 90 per cent. of all people are honest and that, by observation, the dishonest ones can be discerned. This policy is used by small firms in which the

1. *This Survey was conducted by Robert R. Glover in 1933-34.*

proprietors have personal dealings with the customers. It is safe to say that the extent to which it is used is gradually decreasing. The average store using it does approximately one third of its business on credit. About 15 per cent. of the capital of this type of store is in accounts receivable. Bad debt losses amount to about one per cent. of net sales. When one considers recent business conditions, such losses are not excessive. This result is the most important criterion of measurement and is very favourable to this method. There are, however, criticisms. Not enough importance is put on the customer's ability to pay, and it is questionable whether, from observation, one person can judge another by appearance. It must be recognized, that because stores using this method are usually operated by proprietors who know their entire clientele well, the percentage of credit business does not get out of hand. It must also be recognized, because of the small bad debt losses, that the plan is efficient.

A Free Credit Policy Has an Average Loss of 2 Per Cent.

A business following the policy of free credit places greatest emphasis on sales volume. All the firm's policies are directed toward this end. With such emphasis on volume, percentage profits and payment of accounts are relegated to a minor position. Credit is, therefore, given to anyone in an effort to gain a larger volume of sales. The theory admits that bad debt losses will be great, but assumes that the constantly increasing sales volume will yield profits that will more than cover those losses. The average cost of this type of credit is two per cent. of net sales. It is considered advisable to cover this cost, and take an occasional loss, in order to increase sales approximately one third, thus reducing the percentage costs of the burden expenses.

This policy is used by large businesses which make the free credit angle their most important selling point. It is often combined with the instalment sales plan and is usually used in clothing, furniture and radio stores. Other stores selling a relatively high unit value product find it satisfactory. The high unit value would perhaps obviate purchase entirely, or at least defer it, were cash payment insisted upon.

In operation, when a request for credit is received, the credit manager makes an investigation into the applicant's position. The store with a free credit policy will take a greater risk in extending credit, because its theory holds that even the doubtful risks are worth taking,

and indeed must be taken, to make the policy work consistently. The terms allowed are usually from ten weeks to one year. There are very few risks that are refused and therefore the free credit policy is worthy of its name.

The average store of this type does approximately 85 per cent. of its business on credit. The method is very successful in gaining volume. In comparison with similar stores following a stricter credit policy, their sales volume is approximately 100 per cent. greater. About 50 per cent. of the capital of the free credit store is tied up in accounts receivable. The average loss on bad debts under this policy is 1½ to 2 per cent. of net sales.

The theory may be attacked on several counts. The quality of sales is unduly subordinated to the quantity of sales. The increase in sales volume to cover the previous year's debt losses cannot be consistent, for a limit will be reached eventually. Cyclical fluctuations will cause temporary declines in sales. The theory assumes that customers attracted will be a cross-section of the public, and therefore only a small percentage will be dishonest. Actually, however, a large majority cannot get credit elsewhere. It also assumes that there will be continual increases in profits from increasing sales, which assumption is unfounded; for there is a definite point beyond which greater economies from mass output cannot be achieved. Theoretically, also, this plan may be criticized, because the foundation for normal credit is "an equal amount of future goods or profits with which to liquidate the debt."

In defense of the policy, it may be said that it is designed for a class of people who are inherently honest, have small income, large families, and are anxious to keep their jobs. They are worthwhile customers. The system does work, therefore, not on the grounds put forth by the theory, but on other supplementary bases which fortunately happen to exist.

The Strict Credit Policy

The name strict credit policy is properly a "supervised" policy. Inasmuch as it is directly opposite to the free credit policy just described, the name strict credit is considered more appropriate. The theory of this method is that it is unprofitable to sell for credit unless the credit offered is as good as its cash equivalent.

Approximately 65 per cent. of all the businesses studied in the analysis follow this policy. The credit manager makes the decision regarding the advisability of granting credit. Only the best applicants are allowed credit.

Under this plan about 35 per cent. of the total sales are for credit. The average amount of capital tied up in accounts receivable is 13 per cent. The average loss on bad debts is 4/5 of one per cent.

There are no points which can be brought forth to criticize this theory, for actual results show how successful it is. The only caution that might be given is that credit should not be so strict that it results in a turning away of good credit risks, thus restricting sales.

Summary

A scientific system of free credit carefully operated, with stable conditions, may prove successful. By following a more strict method, however, with no unnecessary risks, a business can be reasonably sure of the success of its credit policy. The free credit method, then, is eliminated for the average store as a satisfactory basis for building and operating a business. The inconsistent policy is declining in use and can be used successfully only by the most experienced business men. The strict or supervised plan is, therefore, to be preferred, because it is least costly, least risky, and fundamentally soundest.

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